SEP 24 2003

No. 02-1856

In the Supreme Court of the United States

APPLIED COMPANIES, INC., PETITIONER

v.

DONALD H. RUMSFELD, SECRETARY OF DEFENSE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether petitioner is entitled to an award of anticipatory profits as a result of the government's negligent estimation of the amount of goods subject to a requirements contract, which, if allowed in this case, would put petitioner in a better position than if the contract had not been breached.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-38a) is reported at 325 F.3d 1328. A previous opinion of the court of appeals (Pet. App. 41a-74a), which was subsequently withdrawn, is reported at 318 F.3d 1317. The opinions of the Armed Services Board of Contract Appeals (Pet. App. 75a-93a, 94a-97a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on December 10, 2002. A petition for rehearing was granted and the court of appeals granted a panel rehearing, withdrew the initial panel decision, and issued a substituted decision on April 2, 2003. The petition for a writ of certiorari was filed on June 20, 2003. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case involves a requirements contract entered into by petitioner and the Defense Logistics Agency (DLA), a component of the United States Department of Defense, for cylinders to store R-12 and R-114 refrigerants, which are classified as Class I Ozone Depleting Substances, or ODSs. DLA was charged with building and maintaining a stockpile of ODSs for the Department of Defense. DLA assessed the existing inventories of ODSs, the amount of ODSs likely to be used and recycled, and the amount of ODSs needed to ensure availability for mission critical uses. In June 1993, based on the foregoing assessment, DLA developed estimates of the amount of R-12 and R-114 refrigerants that it needed to acquire to fulfill its mission and the number of cylinders required to store those refrigerants. Pet. App. 5a.

In July 1993, DLA issued a Request for Proposals (RFP) for the acquisition of the necessary cylinders. The RFP estimated that 62,945 cylinders would be needed for the storage of R-12 refrigerants, and that 56,550 cylinders would be needed for the storage of R-114 refrigerants, for a total of approximately 120,000 cylinders during the proposed one-year period of the contract. In August 1993, petitioner responded to the RFP and was the lowest responsive offeror. In January 1994, DLA determined that the reserve requirements for R-12 and R-114 refrigerants were much lower than previously believed and, as a result, the amounts of R-12 and R-114 storage cylinders needed during the forthcoming year were considerably less than believed —2555 and 1037, respectively. Pet. App. 5a-6a.

In June 1994, DLA awarded the requirements contract to petitioner, accepting its bid of $52.60 per

cylinder. The contract—which repeated the (erroneous) estimates contained in DLA's original RFP—obligated DLA to "order from the contractor all the [cylinders] that are required to be purchased by the Government." Pet. App. 6a. The contract incorporated various clauses from the Federal Acquisition Regulations (FAR), including the standard requirements clause. *Id.* at 6a-7a, 80a. The requirements clause provides, in pertinent part, that "[t]he quantities of supplies or services specified in the Schedule are estimates only and are not purchased by this contract." 48 C.F.R. 52.216-21(a).

In August 1994, DLA informed petitioner for the first time that it had "discovered that a significant mistake was made in calculating the estimates." Pet. App. 7a. DLA provided new estimates of the minimum and maximum quantities of R-12 and R-114 refrigerant cylinders that it would require and DLA eventually purchased approximately 11,950 units of R-12 and R-114 cylinders, about one tenth of the quantity originally estimated. *Ibid.*

DLA sought to modify the contract to reflect the new estimates, but the parties were unable to agree to terms and, in February 1995, DLA terminated the contract for convenience of the government. Pet. App. 7a. Petitioner submitted a settlement proposal in the amount of $1,791,499 to account for the shortfall in the cylinders ordered by DLA and the overhead it allegedly absorbed in the course of preparing for and performing its obligations pursuant to the contract. *Ibid.* In February 1997, the termination contracting officer unilaterally settled petitioner's termination claim for $295,253, which included petitioner's costs of terminating its work in progress and $31,718 profit relating to work in progress. *Id.* at 7a-8a.

Petitioner submitted to the termination contracting officer claims for breach of contract, seeking, *inter alia*, anticipatory profits in the amount of $1,057,530. Pet. App. 8a. In June 1998, the contracting officer issued a final decision denying petitioner's claim for anticipatory profits. *Ibid.*

2. Petitioner appealed to the Armed Services Board of Contract Appeals (Board). On cross-motions for summary judgment, the Board held that DLA's negligence in arriving at the erroneous estimates constituted a breach of the contract for which petitioner was entitled to compensatory damages. Pet. App. 75a-97a; see *id.* at 92a. In addition, the Board observed that such damages may include "anticipatory profits," but the Board did not determine any amount of damages and instead indicated that there would be a future "quantum" phase. *Id.* at 92a. The Board denied the government's motion for reconsideration, stating that because DLA's breach was "total," petitioner "is entitled to be made whole, and here that includes anticipatory profits to the extent they can be proved." *Id.* at 97a; see *id.* at 94a-97a.

3. The Federal Circuit affirmed the Board's ruling that the government breached the contract by negligently over-estimating its actual requirements, but concluded that such a breach does not entitle petitioner to an award of anticipatory profits. Pet. App. 1a-38a (substituted opinion).*

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* Petitioner argued that, because the Board did not adjudicate any final judgment on the damages issue, the Federal Circuit lacked jurisdiction over the government's appeal pursuant to 28 U.S.C. 1295(a)(10). The Federal Circuit rejected that argument on the ground that "the Board's decision on entitlement is final and appealable," even though the Board did not finally resolve the damages issue. Pet. App. 10a-11a n.3.

a. The court of appeals emphasized that the "general rule" is that a non-breaching party is not entitled to be put in a better position than if the breaching party had fully performed. Pet. App. 16a-17a. The court recognized that a contracting party may recover lost profits when the government breaches a requirements contract by failing to use the contractor to meet the government's actual requirements and instead diverting the government's business to another entity. *Id.* at 23a. But, the court found, this case does not involve that "kind of breach." *Ibid.* In this case, the court explained, the government did not "divert from a requirements contractor business that existed. To the contrary, [DLA] did order from [petitioner] all of its actual requirements for refrigerant cylinders, although those requirements were far less than what had been estimated in the RFP." *Id.* at 24a. "No case has been cited to us," the court stated, "in which, under a requirements contract, a contractor was allowed to recover anticipatory profits as damages for [such] a breach." *Ibid.*

The court further explained that, ordinarily, "in order to recover anticipatory profits, it must be 'definitely established' that without the government's breach there would have been a profit." Pet. App. 24a (citation omitted). The court found that petitioner "cannot meet that requirement," because, if DLA had "discharged its duty by properly preparing and propounding the cylinder estimates, or if it had told offerors that the estimates were inaccurate before [the] contract award, [petitioner] would not have expected to sell, and it would not have sold, 120,000 cylinders." *Id.* at 24a-25a. Furthermore, the court emphasized, "awarding [petitioner] damages in the form of lost profits would allow [petitioner] to profit from DLA's breach." *Id.* at 25a. "To the extent that it is allowed to recover a profit

based upon the 120,000 units of cylinders included in DLA's negligently prepared estimates, [petitioner] would find itself in a better pecuniary position than if DLA had never propounded the inflated estimates and breached the contract." *Ibid.* "[S]uch a damages award," the court held, "would squarely conflict with the rule that a non-breaching party 'should on no account get more than would have accrued if the contract had been performed.'" *Ibid.* (citation omitted).

At the same time, the court of appeals recognized that, under existing case law, petitioner may be entitled to an award of damages in the form of an equitable adjustment of the contract price to the extent petitioner could demonstrate that it had detrimentally relied upon the government's erroneous estimates in establishing the cost of its goods. Pet. App. 25a-28a. Therefore, the court concluded that, "[i]f any cylinders were delivered, [petitioner] should have the opportunity to establish that it is entitled to an equitable adjustment in the price of those cylinders because it relied on DLA's negligent estimates and, as a result, suffered damages." *Id.* at 28a.

b. Judge Dyk concurred in part and dissented in part. Pet. App. 30a-38a. He agreed with the panel that the government breached the contract by negligently estimating its requirements, but disagreed with its holding on damages. Judge Dyk concluded "that there is no controlling precedent in this area," but, drawing from "the general law of contracts," he would have held that petitioner is entitled to an award of anticipatory profits. *Id.* at 33a; see *id.* at 35a.

4. Petitioner filed a petition for rehearing. The court of appeals granted panel rehearing for the limited purpose of correcting possible factual misstatements in the panel's decision concerning the extent to which any

deliveries were actually made under the contract, withdrew the panel's decision and issued a substituted decision that accounts for any such misstatements, and denied the petition in all other respects. Pet. App. 3a-4a.

ARGUMENT

Petitioner argues (Pet. 5-9) that it was entitled to an award of anticipatory profits for the government's breach of contract in over-estimating its requirements. The court of appeals correctly rejected that argument and found that allowing such damages would place petitioner in a "better pecuniary position" (Pet. App. 25a) than if no breach had occurred. The court's decision does not conflict with any decision of this Court or of any other court of appeals. Indeed, even the dissent below stated that no prior decision has "specifically addressed" the damages issue here. *Id.* at 35a. The petition should be denied.

1. The court of appeals correctly concluded that petitioner is not entitled to an award of anticipatory profits for the government's breach in estimating its requirements. The contract between DLA and petitioner contained an estimate of the government's requirements for the cylinders subject to the contract. Pet. App. 6a-7a, 80a. The contract's requirements clause specifically stated that the quantities specified in the contract were "estimates only," were "not purchased by th[e] contract," and thus did not represent a guarantee that the government would order the estimated amount. 48 C.F.R. 52.216-21(a). Although the court of appeals found that the government negligently inflated its estimates, the court correctly held that such a breach does not entitle petitioner to "the profit it would have made on the entire quantity of * * * [specified merchandise] that DLA negligently estimated it would

require." Pet. App. 16a. As the court explained, awarding petitioner such profits would improperly place petitioner in a better position than if the government had not breached the contract—*i.e.*, if it had accurately stated its estimates. *Id.* at 25a. In addition, allowing such damages would transform the requirements contract in this case into a contract that guaranteed a certain level of business, in direct contravention of the requirements clause quoted above. See *id.* at 80a.

2. That result does not conflict with any other decision of any court of appeals. As the court of appeals explained, although in some instances courts have concluded that a contracting party may recover anticipatory-profit damages from the government due to a breach of a requirements contract, those cases have all involved situations in which the government did not fill its actual requirements by purchasing goods from the contractor, but instead inappropriately diverted its business to other parties. See Pet. App. 18a-24a (discussing *Locke* v. *United States*, 283 F.2d 521 (Ct. Cl. 1960); *Torncello* v. *United States*, 681 F.2d 756 (Ct. Cl. 1982); and *Ace-Federal Reporters, Inc.* v. *Barram*, 226 F.3d 1329 (Fed. Cir. 2000)). In this case, however, the government did not purchase any of its actual requirements from another source. Rather, it negligently over-estimated its actual requirements in contracting with petitioner. Pet. App. 23a-24a. As the court of appeals stated, petitioner has identified "[n]o case * * * in which, under a requirements contract, a contractor was allowed to recover anticipatory profits as damages for a breach of contract resulting from negligently prepared estimates." *Id.* at 24a.

3. Petitioner argues that the decision in this case conflicts with the general legal principles that govern

claims for breach of contracts to which the United States is a party, and asserts "that contracts of the United States are subject to the same law that governs the contracts of private parties." Pet. 5. The decisions cited by petitioner, however, simply recognize that "[w]hen the United States enters into contract relations, its rights and duties therein are governed *generally* by the law applicable to contracts between private individuals." *Mobil Oil Exploration & Producing S.E., Inc.* v. *United States*, 530 U.S. 604, 607-608 (2000) (quoting *United States* v. *Winstar Corp.*, 518 U.S. 839, 895 (1996), and *Lynch* v. *United States*, 292 U.S. 571, 579 (1934)); see *Perry* v. *United States*, 294 U.S. 330, 352 (1935) ("[w]hen the United States, with constitutional authority, makes contracts, it has rights and incurs responsibilities similar to those of individuals who are parties to such instruments"). The decision in this case does not in any way disturb that well-settled principle.

In any event, the decision below is consistent with the general principles governing the award of damages for breach of a contract between private parties. Indeed, as the court of appeals observed, a cardinal principle of contract law is that the non-breaching party is not entitled to be placed in a better position than it would have occupied had the breach not occurred. Pet. App. 17a (citing *Miller* v. *Robertson*, 266 U.S. 243 (1924); *Wells Fargo Bank* v. *United States*, 88 F.3d 1012 (Fed. Cir. 1996), cert. denied, 520 U.S. 1116 (1997); and *White* v. *Delta Constr. Int'l, Inc.*, 285 F.3d 1040 (Fed. Cir. 2002)). As the court explained, if DLA had properly estimated its requirements—*i.e.*, if no breach had occurred—petitioner would not have expected to sell 120,000 cylinders. Pet. App. 24a–25a. Thus, awarding petitioner the profits it allegedly would have

earned if it had sold 120,000 cylinders—more than ten times the amount of the government's actual requirements—would place petitioner in a much better position than it would have occupied if there had been no breach. Nothing in the general law of contracts entitles petitioner to such a windfall.

The Uniform Commercial Code (UCC) is not to the contrary. Although petitioner refers (Pet. 9, 11) to UCC provisions concerning express warranties, it ignores the fact that estimates in requirements contracts have never been considered to be "guarantees or warranties of quantity." *Shader Contractors, Inc.* v. *United States*, 276 F.2d 1, 7 (Ct. Cl. 1960). Indeed, the contract in this case incorporated the standard requirements clause, which, as noted, specifies that estimates are "estimates only," 48 C.F.R. 52.216-21(a), and therefore do not establish any promise or warranty as to actual quantities purchased. Pet. App. 44a, 80a. In any event, even if petitioner could identify a relevant provision of the UCC, the UCC is generally not binding with respect to government contracts. See *Technical Assistance Int'l, Inc.* v. *United States*, 150 F.3d 1369 (Fed. Cir. 1998).

Petitioner's reliance on the Restatement (Second) of Contracts (1981) is also unavailing. See Pet. 8-9. The Restatement (Second) of Torts expressly states that reliance damages, not anticipatory profits, are the appropriate measure of damages for misrepresentation in the contract context. *Id.* § 552B(2) (1977) (*Damages for Negligent Misrepresentation*); see *Womack* v. *United States*, 389 F.2d 793, 800 (Ct. Cl. 1968). Indeed, petitioner appears to recognize as much. Petitioner states that the government's pre-award misstatement of fact was not a breach of contract, but rather a misrepresentation. Pet. 10. Petitioner fails to mention,

however, that the provision cited in its brief would limit its damages for such misstatement of fact to reliance-based damages, not anticipatory profits. Restatement (Second) of Torts, *supra*, § 552B(2).

4. The court of appeals' decision does not leave petitioner without a remedy. The contracting officer unilaterally settled petitioner's termination claim for $295,253, which covered petitioner's costs of terminating its work in progress and $31,718 for profit relating to work in progress (amounts for which petitioner had already received payment under the contract). Pet. App. 7a-8a. Moreover, the court of appeals held that, to the extent that any cylinders were actually delivered, petitioner "should have the opportunity to establish that it is entitled to an equitable adjustment in the price of those cylinders because it relied on DLA's negligent estimates and, as a result, suffered damages." *Id.* at 28a. But the court of appeals correctly rejected petitioner's demand for a $1 million windfall in the form of an anticipatory-profits award.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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